

***United States Court of Appeals
for the Second Circuit***



APPELLEE'S BRIEF

Signed

76-4112

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

ESTATE OF LUDWIG NEUGASS, DECEASED,
HERBERT MARX, JACQUES COE, JR. and
CHASE MANHATTAN BANK, N.A., EXECUTORS,

Appellants

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellee

ON APPEAL FROM THE DECISION OF THE
UNITED STATES TAX COURT

BRIEF FOR THE APPELLEE

SCOTT P. CRAMPTON,
Assistant Attorney General,

GILBERT E. ANDREWS,
GARY R. ALLEN,
JOHN A. DUDECK, JR.,
Attorneys,
Tax Division,
Department of Justice,
Washington, D. C. 20530.

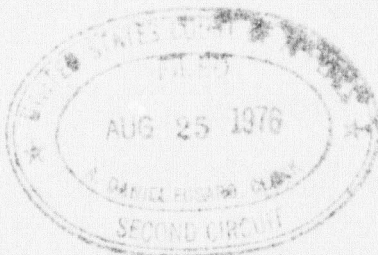


TABLE OF CONTENTS

	Page
Statement of the issue presented-----	1
Statement of the case-----	2
Summary of argument-----	6
Argument:	
The Tax Court correctly held that the interest in decedent's estate passing to the surviving spouse under Article FIFTH of the will was a nondeductible terminable interest under Section 2056(b)(1)-----	10
A. Since absolute ownership of the art objects failed to vest in Mrs. Neugass at the moment of decedent's death, the Tax Court properly concluded that the bequest was a "nondeductible terminable interest"-----	10
1. The background and legislative history of the terminable interest rule-----	11
2. The instant bequest falls within the general terminable interest rule of Section 2056(b)(1)---	15
3. The decision here is in accord with the controlling federal court decisions-----	18
B. The Tax Court's decision in <u>Estate of Mackie v. Commissioner</u> is contrary to the controlling federal legal principles-----	25
C. The extrinsic evidence presented by taxpayers with respect to decedent's intent has little or no bearing on the issue presented-----	32
Conclusion-----	41
Appendix A-----	43
Appendix B-----	45

CITATIONS

Cases:

<u>Allen v. United States</u> , 359 F. 2d 151 (C.A. 2, 1966), cert. denied, 385 U.S. 832 (1966)-----	8, 10, 13, 20, 22, 23, 24, 25, 26, 35, 40
<u>Cuha's Estate v. Commissioner</u> , 279 F. 2d 292 (C.A. 9, 1960), cert. denied, 364 U.S. 942 (1961), rehearing denied, 368 U.S. 870 (1961)-----	18
<u>Flyer, Matter of</u> , 53 Misc. 2d 476, 279 N.Y.S. 2d 76 (Surr. Ct., 1967)-----	22
<u>Fried, In re Estate of</u> , 445 F. 2d 979 (C.A. 2, 1971), aff'g, 54 T.C. 805 (1970), cert. denied, 404 U.S. 1016 (1972)-----	32
<u>Hamilton National Bank of Knoxville v. United States</u> , 353 F. 2d 930 (C.A. 6, 1965), cert. denied, 384 U.S. 939 (1966)-----	31
<u>Hardenbergh v. Commissioner</u> , 198 F. 2d 63 (C.A. 8, 1952)-----	37
<u>Hennessy v. Patterson</u> , 85 N.Y. 91 (1881)-----	21
<u>Jackson v. United States</u> , 376 U.S. 503 (1964)---	11, 18, 19, 20, 23, 24, 26, 30, 39
<u>Jacobsen, Matter of</u> , 61 Misc. 2d 317, 306 N.Y.S. 2d 290 (Surr. Ct., 1969), aff'd, 33 App. Div. 2d 760, 306 N.Y.S. 2d 297 (Sup. Ct., 1969)-----	22
<u>Mackie, Estate of v. Commissioner</u> , 64 T.C. 308 (1975)-----	7, 8, 25, 27, 28, 30
<u>Mittleman v. Commissioner</u> , 522 F. 2d 132 (C.A. D.C., 1975)-----	35
<u>Morgan v. Commissioner</u> , 309 U.S. 78 (1940)-----	35
<u>Northeastern Nat. Bank v. United States</u> , 387 U.S. 213 (1967)-----	39, 40
<u>Opal, Estate of v. Commissioner</u> , 54 T.C. 154 (1970), aff'd, 450 F. 2d 1085 (C.A. 2, 1971)--	33
<u>Pipe's Estate v. Commissioner</u> , 241 F. 2d 210 (C.A. 2, 1957), cert. denied, 355 U.S. 814 (1957)-----	38
<u>Ray, Estate of v. Commissioner</u> , 54 T.C. 1170 (1970)-----	22, 23, 24, 26

Cases (continued):

Reilly's, Estate, In re, 239 F. 2d 797 (C.A. 3, 1957)-----	13
Rudnick, Estate of v. <u>Commissioner</u> , 36 T.C. 1021 (1961)-----	18
Tilyou, Estate of v. <u>Commissioner</u> , 470 F. 2d 693 (C.A. 2, 1972)-----	35
Trunk, Estate of v. <u>Commissioner</u> , 65 T.C. 230 (1975)-----	34

Statutes:

Estates, Powers and Trusts Law, McKinney's Consol. Laws of N.Y. Ann.:	
§ 6-4.10-----	21, 29
§ 6-5.3-----	21
§ 10-3.1-----	21
Internal Revenue Code of 1939, Sec. 812 (26 U.S.C. 1952 ed.)-----	11
Internal Revenue Code of 1954 (26 U.S.C.):	
Sec. 2013-----	39
Sec. 2056-----	10, 43

Miscellaneous:

96 C.J.S., Wills:	
Sec. 925-----	26
Sec. 1148-----	31
H. Rep. No. 1137, 83d Cong., 2d Sess., p. 92 (3 U.S.C. Cong. & Adm. News (1954) 4017, 4118-4119)-----	39
14 New York Jurisprudence, Decedents' Estates:	
§§ 177-189-----	28
§§ 191-200-----	28
Practice Commentary, Estates, Powers and Trusts Law, McKinney's Consol. Laws of N.Y. Ann., § 6-5.3 (1975-76 Pocket Part)-----	21
Rev. Rul. 76-166, 1976-18 Int. Rev. Bull. 17----	30
S. Rep. No. 1013, Part 2, 80th Cong., 2d Sess., pp. 24-29 (1948-1 Cum. Bull. 285, 303-306)----	11, 12, 19
S. Rep. No. 1013, Part 2, 80th Cong., 2d Sess., pp. 4, 7, 9, 11, 12, (1948-1 Cum. Bull. 331, 334, 336, 337, 338-339)-----	13, 17, 28, 29, 30, 38
Treasury Regulations on Estate Tax (26 C.F.R.):	
§ 20.2056(b)-4-----	30
§ 20.2056(b)-5-----	17

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 76-4112

ESTATE OF LUDWIG NEUGASS, DECEASED,
HERBERT MARX, JACQUES COE, JR. and
CHASE MANHATTAN BANK, N.A., EXECUTORS,

Appellants

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellee

ON APPEAL FROM THE DECISION OF THE
UNITED STATES TAX COURT

STATEMENT OF THE ISSUE PRESENTED

Decedent's will provided for a bequest to his surviving spouse of a life interest in his extensive art collection with an option to elect to take absolute ownership of any part of such collection exercisable at any time within six months after his death. The widow exercised this option with respect to a large part of the collection, and the estate sought to include the value of such portion in the marital deduction claimed for federal estate tax purposes under Section 2056 of the Internal Revenue Code of 1954. The question presented is whether the Tax Court correctly disallowed this portion of the claimed marital

deduction on the grounds that the interest in the art collection passing to the widow under the will was one which would terminate or fail on the lapse of time or the occurrence or nonoccurrence of an event or contingency and which therefore constituted a non-deductible terminable interest under Section 2056(b)(1) of the Code.

STATEMENT OF THE CASE

This is an appeal from the decision of the United States Tax Court determining a deficiency in federal estate taxes in the amount of \$109,079.42 against the estate of Ludwig Neugass.

(R. 147.)^{1/} The opinion of the Tax Court, filed October 29, 1975 (Honorable C. Moxley Featherston), is reported at 65 T.C. 188.

(R. 128-146.) The Tax Court entered its decision in favor of the Commissioner on January 22, 1976. (R. 147.) Taxpayers' notice of appeal was timely filed on April 16, 1976. (R. 149.) Jurisdiction is conferred on this Court by Section 7482 of the Internal Revenue Code of 1954.

The case involves the marital deduction claimed by the estate under Section 2056 of the Internal Revenue Code of 1954. The material facts, as stipulated by the parties (R. 16-19) and as found by the Tax Court (R. 129-133), are as follows:

Ludwig Neugass (decedent) died testate on February 24, 1969, a domiciliary of New York, New York. At the time of his death, decedent owned a valuable art collection, consisting of 54 paintings,

^{1/} "R." references are to the separately bound record appendix.

6 bronzes, and a number of porcelains and miscellaneous items, (R. 35-40, 42-43.) Decedent was survived by his wife Carolyn, his daughter, Nancy Carouso, and two grandchildren. Herbert Marx, Jacques Coe, Jr., and Chase Manhattan Bank, N.A., were issued letters testamentary by the Surrogate's Court, New York. (R. 16-17, 129-130.)

Decedent's last will and testament was admitted to probate in the Surrogate's Court on April 3, 1969. (R. 16, 130.) After making several specific bequests, the will provided for the disposition of decedent's art collection as follows (R. 21-22):

FIFTH: I direct that if my wife, CAROLYN NEUGASS, survives me, she shall have the life use of all my paintings and other works of art (hereinafter called my "collection"), without bond, and that upon her death my daughter, NANCY CAROUSO, if she is then living, shall have the life use of said collection, without bond. Upon the death of the survivor of my wife and my daughter, said collection shall become the absolute property of the LUDWIG NEUGASS FOUNDATION.

Neither my wife nor my daughter shall be under any duty to insure said collection or any item therein, but if the FOUNDATION shall elect so to insure the proceeds received upon any loss shall become the absolute property of the FOUNDATION, (free of the life use of either my wife or my daughter).

With respect to any item in said collection:

(a) Within six months after the date of my death, either my wife or my daughter may renounce her life use thereof and, if both of them so renounce, the item shall become the absolute property of the FOUNDATION.

(b) Within six months after the date of my death, either my wife or my daughter may elect to take absolute ownership of any item, whereupon said item shall become the absolute property of my wife or my daughter; in the case of my daughter, such election shall take effect if and only when her life use has begun.

(c) At any time after said six months period either my wife or my daughter may terminate her life use of any item and thus accelerate with respect to said item the provisions otherwise effective upon her death.

On July 2, 1969, pursuant to Article FIFTH of decedent's will, Mrs. Neugass elected to take absolute ownership of 46 of the 55 paintings, all of the Meissen porcelains, the 6 bronzes, and 15 miscellaneous pictures. (R. 35-40.) She executed and filed with the Surrogate's Court an "Election Pursuant to Article FIFTH (b) of the Will of Ludwig Neugass," which provided as follows (R. 34):

WHEREAS, under the terms of Article FIFTH of the Will of LUDWIG NEUGASS, deceased, said decedent bequeathed to his wife, CAROLYN NEUGASS, the life use of all of his paintings and other works of art; and

WHEREAS, under the terms of Article FIFTH (b) of said Will, his wife may within six months after the date of said decedent's death, elect to take absolute ownership of any item of his paintings and other works of art, whereupon said item shall become her absolute property.

NOW, THEREFORE, the undersigned, does hereby elect to take absolute ownership of the items of paintings and other works of art of the decedent listed on Schedule A annexed hereto.

Dated: July 2, 1969

/s/ Carolyn Neugass
CAROLYN NEUGASS

On the same day, Mrs. Neugass renounced her life interest in the nine remaining paintings in decedent's art collection, thereby causing her daughter's life estate in these paintings to commence in accordance with Article FIFTH. (R. 41-43.)

On May 22, 1970, the executors filed a federal estate tax return with the District Director of Internal Revenue at Manhattan, New York. On Schedule M of this return, the estate claimed a marital deduction in the amount of \$682,605.12, including \$383,945 for the value of the artworks of which decedent's spouse elected to take absolute ownership. (Ex. A, p. 29.)

The Commissioner determined that the interest passing to the surviving spouse in the works of art under decedent's will was a terminable interest and disallowed \$337,329.88 of the claimed marital deduction. (R. 132-133.) The Tax Court sustained the Commissioner's determination that the bequest did not qualify for the marital deduction because "At the moment of decedent's death, Mrs. Neugass had not made her election to take absolute ownership of any items in the art collection." (R. 135.) Taxpayers appeal from this ruling.

SUMMARY OF ARGUMENT

Section 2056(a) of the Internal Revenue Code of 1954 provides generally for a marital deduction of up to one half of the value of the adjusted gross estate for any interest in property passing from the decedent to the surviving spouse. This deduction, however, is not allowed with respect to a "terminable interest" as defined by Section 2056(b)(1). A terminable interest essentially is one which is subject to a contingency which could cause the interest to fail and thereby pass to a person other than the surviving spouse. It is the position of the Commissioner that the bequest in the instant case is a nondeductible terminable interest within the meaning of Section 2056(b)(1). The legislative history of the terminable interest rule unequivocally shows that Congress intended the provision to be all encompassing with respect to every kind of contingency and condition and it emphasizes the aim of Congress to disallow the marital deduction if any person other than the surviving spouse may, by any possible circumstances under the terms of the bequest, possess or enjoy any part of the surviving spouse's interest in property.

Since Mrs. Neugass' interest in the subject art collection was expressly limited to a life estate if she did not elect to a greater interest in such collection within six months of decedent's death, there is no question that the bequest to Mrs. Neugass under Article FIFTH of decedent's will in the instant case creates an interest which would terminate or fail "on the lapse of time, on the occurrence of an event or contingency, or on the failure of

an event or contingency to occur" within the liberal meaning of Section 2056(b)(1). Accordingly, we submit that the Tax Court's decision that the bequest is a nondeductible terminable interest is in line with the plain language of Section 2056(b)(1) and the controlling court decisions, and that it should therefore be affirmed.

Ignoring the foregoing, taxpayers contend that the instant bequest somehow qualifies for the marital deduction because it is an "alternative bequest" rather than a life estate with a power of appointment as the Tax Court held. We submit that this reasoning is faulty. In the first place, Mrs. Neugass received a life estate in decedent's art collection which was effective at the moment of decedent's death. At the same time, the will gave Mrs. Neugass the right to elect to take absolute ownership of any item in the collection within six months of decedent's death. As the Tax Court noted, this right is clearly akin to a limited power of appointment under New York law. But even assuming arguendo that the will can be characterized as providing for an alternative bequest, Mrs. Neugass' interest thereunder fails to qualify for the marital deduction under this Court's holding in Allen v. United States, 359 F. 2d 151 (1966), cert. denied, 385 U.S. 832 (1966).

Taxpayers rely principally upon the Tax Court's decision in Estate of Mackie v. Commissioner, 64 T.C. 308 (1975), in which that court held that there is no difference between an election granted by the terms of a will and the doctrine of "election"

which enables a surviving spouse to renounce the will in favor of a state statutory right. We believe that the Tax Court in Mackie, which is currently on appeal by the Commissioner to the Fourth Circuit, misread and misapplied this Court's Allen decision. The Tax Court in Mackie also ignored controlling legislative history indicating Congress' intent that the question whether an interest is terminable must be judged according to the express terms of decedent's will and not according to theoretical interests available under state statutes which the surviving spouse did not take. The courts have held that state created rights are unique and merit special consideration in determining their eligibility for the marital deduction. Such considerations simply do not apply in the case of interests created by will, as in the instant case.

Nor is there any merit to taxpayers' contentions that extrinsic evidence should be admitted to determine the intent of the testator. Here the language of the will is clear and unambiguous, giving Mrs. Neugass six months to elect to take absolute ownership of any item in decedent's art collection, and thus, there is no reason to consider extrinsic evidence under New York law. But even assuming that extrinsic evidence should be considered, the record shows that the unorthodox bequest was simply part of a skillfully drafted post-mortem tax planning scheme designed to give Mrs. Neugass "maximum flexibility." It is this "flexibility" itself which demonstrates that the interest passing to decedent's wife was not fixed at the time of decedent's death, but was contingent on subsequent events. Such contingent

transfers plainly do not qualify for the marital deduction whether or not decedent intended or hoped that they would. Finally, it must be noted that the fact that Mrs. Neugass decided to comply with the conditions with respect to part of the property is clearly not controlling since Congress made no provision for deducting that portion of a terminable interest which became nonterminable at sometime, subsequent to decedent's death. Thus, the decision of the Tax Court is correct and should be affirmed.

ARGUMENT

THE TAX COURT CORRECTLY HELD THAT THE INTEREST IN DECEDENT'S ESTATE PASSING TO THE SURVIVING SPOUSE UNDER ARTICLE FIFTH OF THE WILL WAS A NONDEDUCTIBLE TERMINABLE INTEREST UNDER SECTION 2056(b)(1)

- A. Since absolute ownership of the art objects failed to vest in Mrs. Neugass at the moment of decedent's death, the Tax Court properly concluded that the bequest was a "nondeductible terminable interest"

The issue on appeal is whether the Tax Court correctly decided (R. 135) that the bequest to the surviving spouse under Article FIFTH of decedent's will (R. 22) does not qualify for the marital deduction under Section 2056 of the Internal Revenue Code of 1954, Appendix, infra. The specific question is whether the bequest of the art objects in Article FIFTH--which was limited to a life estate unless Mrs. Neugass "elect[ed] to take absolute ownership of any item" within six months of decedent's death--created an interest which would terminate or fail "on the lapse of time, on the occurrence of an event, or contingency, or on the failure of an event or contingency to occur" Sec. 2056(b)(1). It is the position of the Commissioner in the instant case that the claimed deduction was properly denied since the will did not give Mrs. Neugass absolute ownership of any of the objects of art at the moment of decedent's death. Indeed, any other result would be inconsistent with the plain language of Section 2056(b)(1) and its underlying legislative history, as well as this Court's decision in Allen v. United States, 359 F. 2d 151 (1966), cert. denied, 385 U.S. 832 (1966).

1. The background and legislative history
of the terminable interest rule

Section 2056(a) of the Internal Revenue Code of 1954, in general, allows a marital deduction in computing the taxable estate for purposes of the federal estate tax equal to the value of any interest in property which passes from the decedent to the surviving spouse. This deduction was added as Section 812(e) of the Internal Revenue Code of 1939 (26 U.S.C. 1952 ed.) by Section 361(a) of the Revenue Act of 1948, c. 168, 62 Stat. 110. The underlying purpose of this legislation was to equalize the incidence of the federal estate tax among common law property states and community property states. See S. Rep. No. 1013, 80th Cong., 2d Sess., pp. 24-29 (1948-1 Cum. Bull. 285, 303-306); Jackson v. United States, 376 U.S. 503, 510 (1964).

Generally, in a community property state, a married person "owns" (and thus his estate for estate tax purpose includes) only one half of the community property, the other half belonging to his surviving spouse. In order to approximate this result in common law states, Congress granted a marital deduction of up to one half of the adjusted gross estate for the interests in property that pass from the decedent to his surviving spouse. However, a decedent in a community property state cannot by his will affect in any way the surviving spouse's interest in the community property. Thus, to equate the decedent in a common law state with the decedent in a community property state, Congress

required that the interest in property "must pass outright to the surviving or donee spouse." S. Rep. No. 1013, supra, p. 28 (1948-1 Cum. Bull., p. 305).

Thus, Section 2056(b)(1), consistent with the objective of Congress to limit the marital deduction to "outright" bequests, disallows the marital deduction with respect to certain terminable interests. It provides:

(b) Limitation in the Case of Life Estate or Other Terminable Interest.--

(1) General rule.--Where, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate or fail, no deduction shall be allowed under this section with respect to such interest--

(A) if an interest in such property passes or has passed (for less than an adequate and full consideration in money or money's worth) from the decedent to any person other than such surviving spouse (or the estate of such spouse); and

(B) If by reason of such passing such person (or his heirs or assigns) may possess or enjoy any part of such property after such termination or failure of the interest so passing to the surviving spouse;

*

*

*

The legislative purpose behind the terminable interest rule and the three conditions which create a "nondeductible terminable interest" were succinctly summarized in In re Reilly's Estate, 239 F. 2d 797, 799 (C.A. 3, 1957), as follows:

In order to prevent abuse and tax avoidance through the marital deduction, the terminable interest rule was enacted. Broadly, it excepts from the marital deduction any asset of the estate transferred to the spouse which may by any event ultimately pass from the decedent to any other person for less than full consideration in money or money's worth. * * * To be excluded, the property, of which the terminable interest is a part, must under some contingency be liable to pass from the decedent to someone other than the spouse and be possessed and enjoyed by such other person after the surviving spouse. (Emphasis added.)

See also Allen v. United States, supra, pp. 153-154.

The Senate Finance Committee in explaining the concept behind the terminable interest rule (S. Rep. No. 1013, Part 2, 80th Cong., 2d Sess., p. 12 (1948-1 Cum. Bull. 331, 339) specifically noted that the rule applies--

If any person (other than the surviving spouse) or his heirs or assigns may by any possible circumstances under the terms of the bequest possess or enjoy any part of the property in which the surviving spouse's interest is an interest. (Emphasis added.)

And the Senate Committee further emphasized that an interest is deemed to be terminable if it is subject to any kind of condition or contingency (S. Rep. No. 1013, Part 2, supra, p. 7 (1948-1 Cum. Bull., p. 336)):

It is not necessary under such subparagraph (B) that the contingency or event must occur or fail to occur in order to make the interest terminable. Thus a terminable interest under such subparagraph includes an interest bequeathed to the surviving spouse as long as she resides in Washington, D.C. On the other hand, it includes interests which will in all events terminate, such as an estate for the life of the surviving spouse.

Subparagraph (B) is intended to be all encompassing with respect to various kinds of contingencies and conditions. Thus, it is immaterial whether the interest passing to the surviving spouse is considered as a vested interest subject to divestment or as a contingent interest. Subparagraph (B) applies whether the terms of the instrument or the theory of their application are conceived as creating a future interest which may fail to ripen or vest or as creating a present interest which may terminate. The occurrence of a contingency includes the ending of a condition. Thus, an interest given to the surviving spouse as long as she remains unmarried is a terminable interest.

The only exceptions provided in the statute for the denial of the deduction in the case of such contingent bequests are for bequests which are conditioned solely on the survival of the spouse for a period of not more than six months after the decedent's death (Section 2056(b)(3)) and bequests of life estates with unlimited powers of appointment (Section 2056(b)(5)).^{2/} The Tax Court, as we shall demonstrate, correctly analyzed the instant bequest, and correctly concluded that it fell squarely within the language and intendment of the statutory definition of terminable

^{2/} See also Section 2056(b)(6) for a special rule in the case of life insurance and annuity payments with power of appointment in the surviving spouse.

interests, and that it plainly failed to fall within the statutory exceptions to the general rule of Section 2056(b)(1).

2. The instant bequest falls within
the general terminable interest
rule of Section 2056(b)(1)

Applying Section 2056(b)(1) to the instant bequest, it is clear that all three conditions of the terminable interest rule are present in Article FIFTH, which provides in pertinent part (R. 21-22):

FIFTH: I direct that if my wife, CAROLYN NEUGASS, survives me, she shall have the life use of all my paintings and other works of art (hereinafter called my "collection"), without bond, and that upon her death my daughter, NANCY CAROUSO, if she is then living, shall have the life use of said collection, without bond. Upon the death of the survivor of my wife and my daughter, said collection shall become the absolute property of the LUDWIG NEUGASS FOUNDATION.

* * *

With respect to any item in said collection:

* * *

(b) Within six months after the date of my death, either my wife or my daughter may elect to take absolute ownership of any item, whereupon said item shall become the absolute property of my wife or my daughter; in the case of my daughter, such election shall take effect if and only when her life use has begun.

Clearly, the life estate given to Mrs. Neugass under the first paragraph of Article FIFTH is by its very nature, a nonqualifying terminable interest in the art collection in question. Moreover, Article FIFTH (b), giving Mrs. Neugass a limited power to claim a greater estate, clearly confers no interest which will not

terminate "on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur." The bequest in Article FIFTH (b), by its express terms, is plainly one which would automatically expire "on the lapse of time" six months after the date of decedent's death on August 24, 1969, in the absence of affirmative action by Mrs. Neugass to take absolute ownership, and, by the same token, one which would fail "on the occurrence of an event or contingency or on the failure of an event or contingency to occur"--i.e., Mrs. Neugass' intentional or unintentional failure to elect absolute ownership.

The second condition under the terminable interest rule (Section 2056(b)(1)(A)) is also satisfied, since, in the event Mrs. Neugass failed to "elect to take absolute ownership of any item," her interest would be limited to a life estate and the property would pass for less than adequate and full consideration in money or money's worth to either decedent's daughter or to the Ludwig Neugass Foundation. (R. 21-22.) And finally, by reason of such passing, the third condition under Section 2056(b)(1)(B) is met, since persons other than Mrs. Neugass would then possess or enjoy the property.

It is thus clear that the bequest to Mrs. Neugass in ~~Article~~ FIFTH (b) meets all three requirements of the terminable interest rule. Accordingly, we submit that the Tax Court's holding (R. 135) that the bequest "is a terminable interest and does not qualify for the marital deduction" is in line with the plain language of Section 2056(b)(1) and the overwhelming evidence that Congress intended the terminable interest rule to be "all encompassing with respect to various kinds of contingencies and conditions." S. Rep. No. 1013, Part 2, supra, p. 7 (1948-1 Cum. Bull., p. 336).

The Tax Court also properly concluded that the bequest to Mrs. Neugass did not qualify for the "life estate with power of appointment" exception to the terminable interest rule under Section 2056(b)(5). (R. 140.) This exception applies only if such power "is exercisable by such spouse alone and in all events," and the Regulations unequivocally provide that the power is not "exercisable in all events," if it can be terminated during the life of the surviving spouse "by any event other than her complete exercise or release of it." § 20.2056(b)-5(g)(3), Treasury Regulations on Estate Tax (1954 Code) (26 C.F.R.). Since Mrs. Neugass' "power" was required to be exercised within a period of six months after decedent's death, it was clearly not exercisable "in all events" as required by the Section 2056(b)(5) exception to the terminable interest rule.^{3/}

^{3/} Indeed, taxpayers do not challenge the aspect of the Tax Court's decision--yet, while apparently conceding that an

3. The decision here is in
accord with the controlling
federal court decisions

Although there once existed considerable confusion with respect to the point in time when the contingency requirement of the terminable interest rule would be applied, the issue was settled by the Supreme Court in Jackson v. United States, 376 U.S. 503 (1964). In Jackson, the Court resolved the conflict existing between those courts which had allowed a marital deduction for widow's allowance if the right to the allowance had become unconditionally vested at the time of the probate court decree (e.g., Estate of Rudnick v. Commissioner, 36 T.C. 1021 (1961)), and other courts which had denied the deduction if the right was not unconditionally vested at the time of decedent's death (e.g., Cunha's Estate v. Commissioner, 279 F. 2d 292 (C.A. 9, 1960), cert. denied, 364 U.S. 942 (1961), rehearing denied, 368 U.S. 870 (1961)). In holding that the latter approach was mandated by the legislative history of the marital deduction provision, the Court stated (376 U.S., p. 508):

* * * [It is] the Senate Committee's admonition that in considering terminability of an interest for purposes of a marital deduction "the situation is viewed as at the date of the decedent's death." S. Rep. No. 1013, Part 2, 80th Cong., 2d Sess., p. 10.

3/ (continued)

unlimited power of appointment is necessary to bring the interest within the scope of the statutory exception, their position necessarily implies that a power of appointment which is limited nevertheless somehow brings an otherwise terminable interest outside the scope of the general rule. We submit that Congress could hardly have intended such an anomalous result.

Accordingly, since under California law the widow in Jackson would have lost her allowance if she had died or remarried prior to securing an order therefor, she did not have "an indefeasible interest in property at the moment of her husband's death," and thus acquired at that time only a nondeductible terminable interest under the 1939 Code predecessor to Section 2056.

Jackson v. United States, supra, p. 507.

Applying the Supreme Court's holding in Jackson to the instant bequest, it is clear that Mrs. Neugass did not have an "indefeasible interest in property" at the moment of decedent's death. Jackson v. United States, 376 U.S., p. 507. Instead she had at that time, simply life estate in the art collection with a limited right to elect to take absolute ownership of any item within six months of decedent's death. (R. 21-22.) Thus, at the moment of decedent's death, Mrs. Neugass had, in essence, a life estate with a limited power of appointment, and did not have "outright" ownership of any item in the art collection, as required by the statute. S. Rep. No. 1013, supra, p. 28 (1948-1 Cum. Bull., p. 305). Indeed, by the express terms of Article FIFTH (b), it was necessarily unascertainable whether or not Mrs. Neugass would choose to "elect to take absolute ownership" of all, some, or none of the art objects offered until July 2, 1969, until four months after decedent's death when Mrs. Neugass filed written notices with the surrogate rejecting ownership in nine of the paintings and taking absolute ownership in the remaining art works. (R. 34, 41.) Thus, it could hardly

be contended that the value of the entire art collection (including those items as to which Mrs. Neugass did not exercise her option to claim a greater estate) should be included in the estate's marital deduction, and, as Jackson illustrates, there is simply no statutory provision for allowing the deduction for that portion of the art collection as to which Mrs. Neugass' interest became nonterminable sometime after decedent's death.

The decision of the court below in the instant case is also in accord with the holding of this Court in Allen v. United States, supra, p. 154, that the determination of whether an interest is terminable "is to be judged in the light of events at the precise moment of decedent's death." (Emphasis added.) As Judge Featherston properly concluded (R. 135):

The first sentence of Article FIFTH of decedent's will gave Mrs. Neugass only a life estate in decedent's art collection, and such an estate clearly is a terminable interest.
* * * At the moment of decedent's death, Mrs. Neugass had not made her election to take absolute ownership of any items in the art collection. The bequest, therefore, is a terminable interest and does not qualify for the marital deduction. (Emphasis added.)

Taxpayers nevertheless contend (Br. 18) that the instant bequest qualifies for the marital deduction because it gave Mrs. Neugass "a choice between two alternative gifts."^{4/} We

^{4/} Taxpayers are mistaken in their assertion (Br. 16) that "The Tax Court never dealt with the validity of alternative bequests under New York law." On the contrary, Judge Featherston requested the parties to brief this point and he specifically noted in his opinion that no New York case had been cited "defining the legal standards for distinguishing between a bequest of a life estate plus a power of appointment from a bequest giving the beneficiary

submit that this reasoning is faulty. Here Mrs. Neugass received a life estate in decedent's art collection by the first sentence of Article FIFTH. (R. 21.) No action or choice was required to put that provision into effect since it was effective at the moment of decedent's death. At the same time, the language of Article FIFTH (b) gave Mrs. Neugass the right, limited in duration, to appoint to herself absolute ownership of any item in the art collection. This right--to enlarge a life estate to absolute ownership--is clearly akin to a limited power of appointment. This is supported by the definition of a "power of appointment" under New York law, which defines the term as an authority enabling a donee to designate an appointee of property (Estates, Powers and Trusts Law, McKinney's Consol. Laws of N.Y. Ann., § 10-3,1):

4/ (continued)

the right to choose between a life estate and absolute ownership." (R. 138.) It is clear, however, that this latter choice would create a "future estate subject to a condition precedent" under New York law since the requirement of choosing would make the estate dependent upon the "occurrence of an uncertain event." Estates, Powers and Trusts Law, McKinney's Consol. Laws of N.Y. Ann., § 6-4.10. Moreover, an "alternative bequest" under New York law creates "Future estates in the alternative" (Estates, Powers and Trusts Law, McKinney's Consol. Laws of N.Y. Ann., § 6-5.3) which are sometimes referred to as "contingencies with a double aspect." Hennessey v. Patterson, 85 N.Y. 91, 99 (1881); See Practice Commentary, Estates, Powers and Trusts Law, McKinney's Consol. Laws of N.Y. Ann., § 6-5.3 (1975-76 Pocket Part). In short, Mrs. Neugass' interest under Article FIFTH is clearly a "contingent interest" under New York law whether it is viewed as a life estate with a power of appointment or as an alternative bequest.

A power of appointment * * * is an authority created or reserved by a person having property subject to his disposition, enabling the donee to designate, within such limits as may be prescribed by the donor, the appointees of the property or the manner in which such property shall be received.

Article FIFTH clearly creates a limited power of appointment under New York law since Mrs. Neugass was given the "authority" for six months to designate herself as the "appointee" of absolute ownership of any item in the art collection. Accordingly, we submit that the court below properly characterized Mrs. Neugass' interest as "a power to appoint to herself," and, as noted above, properly held that since such power was not exercisable "in all events," it did not fall within the power of appointment exception to the terminable interest rule. (R. 138-140.) Regulations § 20.2053(b)-5(g)(3).

But even assuming arguendo that Article FIFTH could be read as conferring alternative bequests, as taxpayers contend (Br. 16), Mrs. Neugass' interest thereunder would still be properly viewed as a "nondeductible terminable interest" under this Court's holding in Allen v. United States, supra, see also Estate of Ray v. Commissioner, 54 T.C. 1170 (1970). Like Matter of Jacobsen, 61 Misc. 2d 317, 306 N.Y.S. 2d 290 (Surr. Ct., 1969), aff'd, 33 App. Div. 2d 760, 306 N.Y.S. 2d 297 (Sup. Ct., 1969), and Matter of Flyer, 53 Misc. 2d 476, 279 N.Y.S. 2d 76 (Surr. Ct., 1967)--which taxpayers cite (Br. 16-18) for the proposition that the New York courts recognize the validity of alternative

bequests--the will in Allen v. United States, supra, provided for alternative bequests to the decedent's surviving spouse. There, in Part I of his will, the decedent provided for a bequest of his entire estate to his surviving spouse on condition that she "'sign and execute an agreement suitable to the Surrogate * * * to make a Will and leave her estate * * * to be shared in equal parts among * * * [decedent's] four children * * *.'" Allen v. United States, supra, p. 153. In the event the required agreement was not executed, Part II of the will alternatively bequeathed to the surviving spouse her statutory share of the estate with the residue going to decedent's daughter by his first marriage. Applying the established principles of Jackson v. United States, supra, this Court held that the bequest was a terminable interest stating (359 F. 2d, p. 154):

* * * it is apparent that the devise runs afoul of the terminable interest rule. Viewed at the moment of his death, the bequest to Allen's spouse under Part I of his will was subject to at least two contingencies, each of which could have caused it to fail: (1) Kathleen might not have elected to take under Part I at all; or, (2) * * * there remained the need for the Surrogate's approval * * *.

Likewise, in Estate of Ray v. Commissioner, the decedent's will made a bequest to the surviving spouse on the condition that he execute and file a certain agreement with the probate court within four months of the decedent's death. The agreement required the surviving spouse, upon his death, to devise to their daughter an amount equivalent in value to that of the wife's bequest to the surviving spouse. 54 T.C., p. 1171. In the event

the required agreement was not executed, the will alternatively bequeathed the property to a trust for the benefit of the daughter. Just as in the instant case, the surviving spouse in Estate of Ray timely filed the required document with the local court and the estate claimed a marital deduction for the bequest. The Tax Court, however, correctly held the bequest to be a terminable interest, reasoning as follows (54 T.C., p. 1173):

Under the terms of the decedent's will the bequest to her spouse was expressly conditional: the bequest would fail if Andrew failed to execute and file a written agreement * * * [as prescribed by the will]. In the event Andrew did not execute the foregoing agreement within 4 months of the decedent's death the bequest was to pass to a trust for their daughter. Thus, under the terms of the bequest the gift would fail upon the passage of 4 months without performance of the conditions of paragraph Fourth. * * * Thus, the provisions of section 2056(b) would appear to disqualify the residuary bequest here in issue for the marital deduction.

Accordingly, under this Court's decision in Allen, supra, and the Tax Court's decision in Estate of Ray, the instant bequest--regardless of whether it is considered an alternative bequest or a life estate with a power of appointment--is not a gift outright, but is expressly conditioned on the performance of an affirmative act by the surviving spouse within a specified period, and thus fails to vest an "indefeasible interest in property" in Mrs. Neugass at the moment of decedent's death. Jackson v. United States, 376 U.S., p. 507.

B. The Tax Court's decision in
Estate of Mackie v. Commissioner
is contrary to the controlling
federal legal principles

Taxpayers concede (Br. 19) that the only case that they have found in support of their position is Estate of Mackie v. Commissioner, 64 T.C. 308 (1975), a case which is currently on appeal by the Commissioner to the Fourth Circuit, No. 76-1206. As demonstrated below, we submit that the Tax Court's decision in Estate of Mackie is contrary to Allen v. United States, supra, and the controlling federal legal principles, and should not be followed in this case.

Estate of Mackie involved the application of the terminable interest rule to a bequest which, like the instant bequest, was expressly conditional and would lapse automatically on the passage of time. Item Nine of the Mackie will provided for a bequest to decedent's wife of property, to be selected by her, equal (when added to other interests passing to her and qualified for inclusion in the marital deduction) to the maximum marital deduction to which the estate might be entitled, but further provided as follows (64 T.C., p. 309):

My said wife shall have, however, the right to elect whether to accept this devise, bequest and appointment, or to reject it, or to accept it in part and reject it in part, which election she shall make by a statement in writing to that effect delivered to my executrix within four months from the date of my death. The failure of my said wife to deliver such statement to my executrix within such time shall be deemed an election by her to reject this devise, bequest and appointment in full.

Three months after decedent's death, Mrs. Mackie delivered a statement of acceptance to the executrix in accordance with the requirements of Item Nine. Since Item Nine--like Article FIFTH (b) in the instant case--created an automatic presumption of rejection, nothing vested in Mrs. Mackie until she delivered the statement of acceptance.^{5/} Thus, the bequest was clearly an example of a terminable interest. Allen v. United States, supra, pp. 154-155; Jackson v. United States, 376 U.S., p. 507.

Nevertheless, the Tax Court in that case held that the bequest to Mrs. Mackie was not a terminable interest, attempting to distinguish the bequests in Allen v. United States, supra, and Estate of Ray, supra, on the grounds that those bequests required the surviving spouse to perform "acts in addition to merely accepting the bequest." 64 T.C., p. 313. On the contrary, however, the Government had specifically argued in Allen that the fact that Mrs. Allen might choose simply to reject the bequest by failing to execute the required agreement was itself an unambiguous and unequivocal contingency causing Part I of the will to be a terminable interest. This Court agreed, specifically pointing out in its opinion that the fact that "Katheleen might not have elected to take under Part I at all" was a separate contingency. 359 F. 2d, p. 154. Similarly, in Estate of Ray, supra, the Tax Court noted that "under the terms of the bequest

^{5/} This is similar to the common law rule that where a will makes the vesting of a bequest dependent upon a contingency, the bequest does not vest until the happening of the contingency. 96 C.J.S., Wills, Sec. 925.

the gift would fail upon the passage of 4 months without the performance of the other conditions." 54 T.C., p. 1173.

But the most fundamental error in the Mackie opinion is the court's statement that there is no difference between an election granted by the terms of a will and the doctrine of "election" which enables a surviving spouse to renounce the will in favor of a state statutory right. The Tax Court stated (64 T.C., pp. 311-312):

What Item Nine of the decedent's will did in effect was to leave her nothing, unless she accepted the bequest in whole or in part. Substantively, Mrs. Mackie was put in the same position as a disinherited surviving spouse who is given a statutory right of election. N.C. Gen. Stat. sec. 30-1 (1966).

In the first place, this statement is a misinterpretation of the Mackie will since Mrs. Mackie was not disinherited if she failed to accept the bequest in Item Nine, as Judge Tannenwald mistakenly assumed.^{6/} But more importantly, the legislative history under Section 2056(b) unequivocally shows that Congress intended to forbid analogies to the widow's right to take against the will under state law where, as here, the widow actually takes under the terms of the will. The Senate Finance Committee outlined

^{6/} If Mrs. Mackie failed to elect absolute ownership of any of the property in the bequest in Item Nine, it simply went to a trust in Item Twelve of the will where Mrs. Mackie had a joint life interest in the trust's income. 64 T.C., pp. 309-310. Taxpayer on appeal in Estate of Mackie has conceded (Br. 39) that "Mrs. Mackie could not have claimed an intestate share under N.C. Gen. Stat. § 30-1(a)," as Judge Tannenwald mistakenly implies in his opinion.

this general rule as follows (S. Rep. No. 1013, Part 2, supra, p. 4 (1948-1 Cum. Bull., p. 334)):

If the surviving spouse takes under the decedent's will, the interest passing to her is determined from the will.

The Senate Committee reiterated this fundamental principle, emphasizing its aim to deny the marital deduction if the surviving spouse decides to take a terminable interest in accordance with the will, even though a marital deduction would have been allowed if she had taken against the will (S. Rep. No. 1013, Part 2, supra, p. 11 (1948-1 Cum. Bull., pp. 338-339)):

If the decedent by his will bequeaths a terminable interest for which a deduction is not allowed and the surviving spouse takes in accordance with the will, the marital deduction is not allowed even though under the local law the interest which such spouse could have taken against the will was a fee interest for which a deduction would be allowed. Any theory that the interest which she could have taken under the local law did pass to her in such a case and was used by her to purchase the interest under the will is contrary to the intended application of this section.

Thus, the underlying premise of the Mackie opinion and taxpayers' position (Br. 20) in the instant case--that there is no difference between an election granted to a widow by the terms of a will and the widow's "right of election" to take against a will pursuant to local law--is contrary to the legislative history of the terminable interest rule and is based upon a misunderstanding of the fundamental principles of the law of wills and future estates. See 14 New York Jurisprudence, Decedents' Estates §§ 177-189,

191-200; Estates, Powers and Trusts Law, McKinney's Consol. Laws of N.Y. Ann., § 6-4.10 (Definition of a future estate subject to a condition precedent).

It is undisputed that Mrs. Neugass chose to take under the terms of her deceased husband's will. Indeed, taxpayers indicated on Schedule M of the estate tax return that Mrs. Neugass did not have the right to take a state created interest. (Ex. A, p. 29.) Thus, in accordance with the clear mandate of the legislative history, the question whether or not Mrs. Neugass took a terminable interest for federal estate tax purposes must be judged according to the express terms of the will and not according to theoretical interests which might otherwise have been available under state statutes. And unlike a statutory right otherwise vested at the moment of decedent's death, Mrs. Neugass' will-created power to appoint to herself "did not purport to relate back to the decedent's death but was effective as of July 2, 1969, the date she executed and filed her election with the Surrogate's Court," as the Tax Court correctly concluded. (R. 139.)^{7/}

^{7/} Nor is there any merit to taxpayers' assertions (Br. 21) that an election within a will is not a disqualifying "event or contingency" within the meaning of the terminable interest rule. As we indicated earlier, the terminable interest rule was intended by Congress to be all encompassing with respect to all kinds of contingencies and conditions. There is no question that Mrs. Neugass' interest in Article FIFTH (b) must be treated as a terminable interest since at the moment of decedent's death both decedent's daughter and the Ludwig Neugass Foundation could "by * * * possible circumstances under the terms of the bequest possess or enjoy * * * part of the property" in question. S. Rep. No. 1013, Part 2, supra, p. 12 (1948-1 Cum. Bull., p. 339).

Thus, the commuted dower cases and similar cases involving the special situation of state created rights, relied on by the Tax Court in Mackie, supra, p. 311, and by taxpayers here (Br. 20-21), are inapplicable to the will created interest involved here. Similarly, the Commissioner's conclusion in Rev. Rul. 76-166, 1976-18 Int. Rev. Bull. 17, 18--that a formal legal requirement pursuant to Arizona statutes that a surviving spouse affirmatively signify acceptance of a statutory right otherwise vested at the moment of decedent's death does not make such state created right conditional for purposes of the terminable interest rule--is not inconsistent with the Commissioner's position with regard to the will created right at issue in the instant case, as taxpayers mistakenly imply. (Br. 22.) Thus, Rev. Rul. 76-166 is but a restatement of the same position that the Government took regarding the special nature of state created rights on brief before the Supreme Court in Jackson v. United States, supra.^{8/}

Moreover, it is clear that, contrary to the clear legislative intent (S. Rep. No. 1013, Part 2, supra, p. 9 (1948-1 Cum. Bull., p. 337)), state created rights could never qualify for the marital deduction if the formal legal requirements necessary to claim the rights were regarded as making such interests conditional for

^{8/} The Regulations relied on by taxpayers (Br. 23-24) with respect to an election by a surviving spouse in a community property state to take an outright bequest under the decedent's will in lieu of her share of community property (Regulations § 20.2056(b)-4, Ex. (3)) are similarly inapposite here where the choice is not simply between interests conferred by state law and interests passing under the decedent's will, but rather an election, exercisable within a limited period, to expand a more limited interest passing under the decedent's will.

purposes of Section 2056(b). Indeed, the cases relied on by taxpayers (Br. 20) implicitly recognize the fact that state created rights are special situations. Thus in Hamilton National Bank of Knoxville v. United States, 353 F. 2d 930, 933 (C.A. 6, 1965), cert. denied, 384 U.S. 939 (1966) the court pointed out:

To hold that an interest is terminable only because legal procedures are invoked to enforce an interest which is otherwise vested at the date of the husband's death, is to hold that all elective rights, such as the widow's allowance and the statutory interest in lieu of dower, are disqualified as marital deductions.

The ministerial legal procedures that a surviving spouse must follow to claim a state created right are comparable to the ministerial procedures that must be followed under state statutes to probate a will. But the condition of acceptance imposed by the decedent upon the bequest to his spouse in the instant case cannot be regarded as a mere ministerial act equivalent to the acceptance of an outright bequest. Indeed, Mrs. Neugass' acceptance of an outright bequest would have been presumed under New York law. See 96 C.J.S., Wills, Sec. 1148(c), p. 943. Decedent, however, chose not to provide in his will for such an outright gift, but, in order, as we show below, to provide an opportunity for Mrs. Neugass to engage in a degree of post-mortem estate planning, chose, instead, to confer on her only a life estate except to the extent she might choose, within six months after his death, to expand her life estate in any particular items to an absolute ownership interest therein. Clearly, there is no

reason to extend to the circumstances of the instant case the special rule applied in the case of elections to take against the will pursuant to statutory rights vesting in the surviving spouse as of the moment of decedent's death, since to do so would require the substantial contingency built into the terms of the bequest to be disregarded, and would result in the allowance of a marital deduction with respect to an interest which did not become nonterminable until several months after the date of decedent's death.

C. The extrinsic evidence presented by taxpayers with respect to decedent's intent has little or no bearing on the issue presented

Despite the plain and unambiguous language of decedent's will, taxpayers contend (Br. 8-16) that the Tax Court erred in failing to give consideration to extrinsic evidence as to the underlying intent of the testator. We submit that this Court's decision in In re Estate of Fried, 445 F. 2d 979 (1971), aff'g, 54 T.C. 805 (1970), cert. denied, 404 U.S. 1016 (1972), dealing with a comparable fact situation, establishes that such extrinsic evidence was properly disregarded.

Fried involved a marital deduction bequest conditioned upon the widow surviving probate. Under New York law, it was likely that probate would take longer than six months, thereby rendering the Section 2056(b)(3) survivorship exception to the terminable interest rule inapplicable. The estate, however, argued that the bequest qualified for the marital deduction, relying on the testimony of the scrivener of the will that the condition was

intended to be part of a common disaster clause. In excluding this testimony, the Tax Court held (54 T.C., p. 816):

Whether this testimony was properly admissible, we need not decide since in our view the language of the will is clear that it provided that the residual estate go to decedent's daughter if his wife died before the probate of the will. * * * Where the provisions of a will are clear and unambiguous, external factors are not to be considered in construing that will under New York law. In Re Bull's Estate, supra [175 Misc. 197, 23 N.Y.S. 2d 5 (Surr. Ct., 1940)], and In re Johnston's Estate, supra [186 Misc. 540, 64 N.Y.S. 2d 543 (Surr. Ct., 1945)].

In affirming the decision of the Tax Court, this Court relied only on the clear language of decedent's will, stating (445 F. 2d, p. 982):

The words of the clause itself, however, indicate that the intent was to create two separate conditions: that the widow not die in a common disaster, and that she not die before probate.

Estate of Opal v. Commissioner, 54 T.C. 154 (1970), aff'd, 450 F. 2d 1085 (C.A. 2, 1971), is also in point. There, the decedent's joint and mutual will devised the residue of his estate to his surviving spouse "absolutely and forever," but thereafter provided that, upon the death of his spouse, the residue of her estate was devised to their son. And as in the instant case, the estate in Opal attempted to use the testimony of the scrivener, the widow, and the son to show the decedent's "intent in writing the will." 54 T.C., p. 159. In denying the marital deduction, the Tax Court in a reviewed opinion held this testimony to be inadmissible stating (54 T.C., p. 160):

The settled law of New York is that express declarations of intention not contained in a will (except in cases of equivocation as to the subject or object of a gift) may never be shown. Matter of Smith, 254 N.Y. 283, 172 N.E. 499 (1930) * * * Insofar as the testimony is designed to reveal or prove Edward's dispositive intentions, it is inadmissible.

Again, this Court affirmed the decision of the Tax Court noting that "The language in the preamble of the joint will is so clear as to render supererogatory any citation of New York authority that a binding contract was created." 450 F. 2d, p. 1086 (Emphasis added.) See also Estate of Trunk v. Commissioner, 65 T.C. 230 (1975), on appeal to this Court, No. 76-4125.

In the instant case, the language of Article FIFTH (b) of the will is clear and unambiguous, giving Mrs. Neugass six months to "elect to take absolute ownership of any item" in decedent's art collection. (R. 22.) Thus, the intention of the testator must be gathered from the clear language of the will, drawn by knowledgeable draftsmen, and extrinsic evidence is not admissible. In short, the only issue here relates to the legal consequences of the unambiguous testamentary language in Article FIFTH (b). And since it is clear that he intended his wife would have more than a life estate in the art collection only to the extent she affirmatively elected to claim absolute ownership of designated items, we submit that the bequest was of a terminable interest within the meaning of Section 2056(b)(1) whether or not decedent intended, or expected, that the marital deduction would be

available to the extent she exercised this option.^{9/} Taxpayers' reliance (Br. 10, 13) on Estate of Tilyou v. Commissioner, 470 F. 2d 693 (C.A. 2, 1972) and Estate of Mittleman v. Commissioner, 522 F. 2d 132 (C.A. D.C., 1975), is clearly misplaced. Unlike the instant case, the District of Columbia Circuit in Mittleman perceived an ambiguity in decedent's will necessitating reliance upon extrinsic evidence. 522 F. 2d, p. 137. Moreover, Mittleman is distinguishable from the instant case since the court there relied upon the local law of the District of Columbia in interpreting decedent's will. And, in Tilyou, this Court held that there was a proper foundation to admit extrinsic evidence to determine the meaning of a phrase in decedent's will which had two possible interpretations under New York law. Unlike Tilyou, there is no uncertainty regarding the meaning of the language of the bequest in the instant case warranting the consideration of extrinsic evidence.

In any event, as the Tax Court noted (R. 142) the extrinsic evidence relied on by taxpayers provides no support for their case. What the record shows is that decedent had no fixed or certain ideas as to how to dispose of the art collection. Instead, his major concern was simply complete flexibility for his spouse. Mr. Rosenberg, the only witness who spoke with decedent concerning his will, testified (R. 74):

^{9/} As we indicated above, Article FIFTH is a terminable interest whether it is viewed as a limited power of appointment or as an alternative bequest under New York law. Allen v. United States, supra. Cf. Morgan v. Commissioner, 309 U.S. 78, 80-81 (1940).

He indicated that he had a huge art collection -- the value of which was known or estimated at that time but the value which in the future was uncertain. And he considered this to be a complicating factor in his estate because with respect to the art, how that-- first of all he didn't know whether he wanted it to go to his wife or set up a foundation for it. He thought he had a -- huge collection which he might want to keep intact. Now what he told her -- what he wanted to do was get as much flexibility with respect to this art collection as possible. (Emphasis added.)

Decedent's lack of any definite intention other than flexibility regarding the collection is also clear from Mr. Rosenberg's memorandum of his meeting with decedent on May 11, 1967. (Ex. D, Appendix B, infra, The memorandum shows that Mr. Rosenberg discussed with decedent a number of possible alternatives ranging from life estates, to outright bequests, to charitable contributions. (Ex. D, p. 2.) After his meeting with decedent on May 11, 1967, Mr. Rosenberg concluded that he and his associates "will have to decide how the art collection should be handled." (Ex. D, p. 2.) The end result was Article FIFTH, which Mr. Rosenberg explained to decedent as follows (R. 75-76):

* * * with respect to the art, I told him that the provisions, although complicated, did accomplish what he wanted in that they did give complete flexibility to his wife with respect to the art. That she could take it herself * * * or if she did not want to have it, she could then -- then the art would be given to his daughter * * * and if neither one wanted the art, then it could go to a charitable foundation * * * free of tax and that the tax on the art would not eat up the rest of the estate * * *.

In short, it is unmistakably clear that the primary purpose of the bequest in Article FIFTH was not to attain the marital

deduction but was to achieve maximum flexibility for Mrs. Neugass with respect to the art collection.

Decedent's concern with achieving maximum flexibility was apparently due to the fact that--as the draftsman of decedent's will, Mr. Lustgarten testified--"Mrs. Neugass had been ill and that the status of her health was uncertain." (R. 86.) See also (Ex. D, p. 2.) Thus, an "outright bequest" to Mrs. Neugass would unduly enlarge her own estate for tax purposes, in view of her uncertain health. Indeed, Mr. Rosenberg's memorandum of his meeting with decedent on May 11, 1967, indicates that he advised Mr. Neugass against the use of outright bequests (Ex. D, p. 2):

I suggested the following alternatives to Mr. Neugass with respect to the art:

a. Outright bequests. I pointed out that this would involve a substantial estate tax cost and would in effect require the estate to "buy back" the paintings.

And as Mr. Lustgarten's testimony indicated (R. 88-91), an "outright bequest" vesting at the moment of decedent's death could result in a costly gift tax in the case where it was later necessary for Mrs. Neugass to renounce part of the bequest. Cf. Hardenbergh v. Commissioner, 198 F. 2d 63 (C.A. 8, 1952). Unlike an "outright bequest," the unorthodox bequest in Article FIFTH avoids any gift tax problems involving a renunciation since it vests only a life estate at the moment of decedent's death. Moreover, as Mr. Lustgarten pointed out (R. 105), the automatic presumption of rejection within six months in Article FIFTH (b) was clearly intended to save Mrs. Neugass' own estate from

extensive gift or estate taxes in the event she was otherwise unavailable to renounce, if that course would become appropriate, because of her precarious health.

Thus, there is clearly no merit in taxpayers' contentions (Br. 7, 15) that an outright bequest was not given to Mrs. Neugass simply because of uncertainties under New York law. Instead the record here overwhelmingly demonstrates that Article FIFTH was part of a skillfully drafted post-mortem tax and estate planning device designed to give Mrs. Neugass "all of the options that * * * [decedent] had during his lifetime vis-a-vis the art collection." (R. 87.) We do not challenge the propriety of this devise, but simply submit that taxpayers cannot have both contingent bequest and a marital deduction at the same time. As we have shown above, the terminable interest rule was "intended to be all-encompassing with respect to various kinds of contingencies." and conditions." S. Rep. No. 1013, Part 2, supra, p. 7 (1948-1 Cum. Bull., p. 336).

Nor is there any merit to taxpayers' argument (Br. 3) that Mrs. Neugass' estate will be subjected to double taxation if the marital deduction is denied. The same argument was rejected by this Court in Pipe's Estate v. Commissioner, 241 F. 2d 210, 214 (1957), cert. denied, 355 U.S. 814 (1957) "because the possibility of double taxation is not a sufficient basis for allowing the marital deduction if the bequest does not comply with the

specific statutory requirements."^{10/} The Supreme Court restated this fundamental principle in Jackson as follows (376 U.S., pp. 509-510):

* * * there is no provision in the Code for deducting all terminable interests which become nonterminable at a later date and therefore taxable in the estate of the surviving spouse if not consumed or transferred. The examples cited in the legislative history make it clear that the determinative factor is not taxability to the surviving spouse but terminability as defined by the statute. [S. Rep. No. 1013, Part 2, 80th Cong., 2d Sess., pp. 10, 11, 15.]

Finally, taxpayers are also mistaken in their reliance (Br. 12) on Northeastern Nat. Bank v. United States, 387 U.S. 213 (1967). Northeastern Nat. Bank involved a 1954 amendment to the life estate with power of appointment exception to the terminable interest rule. See Section 2056(b)(5). Relying on specific legislative history to this amendment, the Supreme Court concluded that Congress intended to afford a liberal estate-splitting possibility in those cases where the spouse was entitled for life to all of the income from a "specific portion" of a trust corpus (here \$300 per month), with a power to appoint such specific portion. 387 U.S., pp. 220-221. H. Rep. No. 1337, 83d Cong., 2d Sess., p. 92 (3 U.S.C. Cong. & Adm. News (1954) 4017, 4118-4119). Since the court was not concerned with the general terminable

^{10/} The effect of the terminable interest rule is, of course, mitigated to some extent by Section 2013 (26 U.S.C.), which allows a partial credit to the surviving spouse for prior federal estate taxes paid.

interest rule of Section 2056(b)(1), which has been unchanged since the original enactment of the marital deduction in 1948, there is no merit in taxpayers' contention (Br. 12) that the Supreme Court's decision in Northeastern Nat. Bank represents an emerging trend away from "strict adherence to the formalities of the marital deduction rules."

Here, of course, there was plainly no such "strict adherence" to the statutory requirements, and, indeed, as the record shows, the concern of the decedent and the draftsman with being "meticulous in adhering to the formal requirements of section 2056" (Allen v. United States, 359 F. 2d, p. 153) was clearly secondary to their concern with the financial planning needs of the estate.^{11/} As in Allen, of course, there is no doubt as to the legitimacy or propriety of the device chosen to give the estate and Mrs. Neugass maximum flexibility with respect to the ultimate disposition of the property in question. But, as in Allen, the flexibility thereby provided is necessarily obtained at the expense of failing to qualify for the marital deduction which would have been available in the case of an outright bequest of such property to the surviving spouse.

^{11/} As the draftsman admitted (R. 952-1002) he did no research at all on the question whether such a novel and unorthodox provision would qualify for the marital deduction.

CONCLUSION

For the reasons stated above, the decision of the Tax Court is correct and should be affirmed.

Respectfully submitted,

SCOTT P. CRAMPTON,
Assistant Attorney General,

GILBERT E. ANDREWS,
GARY R. ALLEN,
JOHN A. DUDECK, JR.,
Attorneys,
Tax Division,
Department of Justice,
Washington, D. C. 20530.

AUGUST, 1976.

CERTIFICATE OF SERVICE

It is hereby certified that service of this brief has been made on opposing counsel by mailing four copies thereof on this 24th day of August, 1976, in an envelope with postage prepaid, properly addressed to them as follows:

Jacob Imberman, Esquire
Alan S. Rosenberg, Esquire
Lawrence J. Rothenberg, Esquire
Benjamin L. Greenberger, Esquire
Proskauer Rose Goetz & Mendelsohn
300 Park Avenue
New York, New York 10022

Gilbert E. Andrews
GILBERT E. ANDREWS,
Attorney.

APPENDIX A

Internal Revenue Code of 1954 (26 U.S.C.):

SEC. 2056. BEQUESTS, ETC., TO SURVIVING SPOUSE

(a) Allowance of Marital Deduction.--For purposes of the tax imposed by section 2001, the value of the taxable estate shall, except as limited by subsections (b), (c), and (d), be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property which passes or has passed from the decedent to his surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

(b) Limitation in the Case of Life Estate or Other Terminable Interest.--

(1) General rule.--Where, on the lapse of time, on the occurrence of an event, or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate or fail, no deduction shall be allowed under this section with respect to such interest--

(A) if an interest in such property passes or has passed (for less than an adequate and full consideration in money or money's worth) from the decedent to any person other than such surviving spouse (or the estate of such spouse); and

(B) if by reason of such passing such person (or his heirs or assigns) may possess or enjoy any part of such property after such termination or failure of the interest so passing to the surviving spouse;

*

*

*

(5) Life estate with power of appointment in surviving spouse.--In the case of an interest in property passing from the decedent, if his surviving spouse is entitled for life to all the income from the entire interest, or all the income from a specific portion thereof, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire interest, or such specific portion (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of others), and with no power in any other person to appoint any part of the interest, or such specific portion, to any person other than the surviving spouse--

(A) the interest or such portion thereof so passing shall, for purposes of subsection (a), be considered as passing to the surviving spouse, and

(B) no part of the interest so passing shall, for purposes of paragraph (1) (A), be considered as passing to any person other than the surviving spouse.

This paragraph shall apply only if such power in the surviving spouse to appoint the entire interest, or such specific portion thereof, whether exercisable by will or during life, is exercisable by such spouse alone and in all events.

*

*

*

PROSKAUER ROSE GOLTZ & MENDLSOHN

OFFICE MEMO

Re: Ludwig Neugass - Will

To: Mr. P. J. Hirsch (cc: Mr. W. H. Friedman)

From: Mr. A. S. Rosenberg

Date: May 11, 1957

Ludwig Neugass is a new client of mine who came in this morning concerning a Will. He advised me that his assets are about \$2,000,000 consisting of paintings currently valued at about \$800,000, porcelain which he has not had currently valued but which is very valuable and other assets worth about \$1,000,000. Attached is a copy of his Will, which was prepared by Kaye, Scholer. The basic plan in the Will is satisfactory except as follows:

1. He would like a simpler document if possible.
2. The amounts payable to the charities in paragraph

Third should be as follows:

- a. Federation, \$7,000.
- b. UJA, \$4,000.
- c. Cancer Committee, \$5,000.
- d. Heart Association, \$5,000.
- e. Tuberculosis, \$2,000.
- f. Kessler Institute, \$1,000.
- g. Deborah Hospital, \$3,000.

Dis Trust.

LN should resign -

Has no dominions Paul?

7 Bonner

3. The bequest in paragraph Fourth (c) should be changed to \$10,000.

5. We will have to decide how the art collection should be handled. The collection consists of paintings by Monet, Chagall, Pascin, Gauguin, Vlaminck and other well known painters (hopefully no forgeries).

Mrs. Neugass is 65 years old and has had two brain tumor operations. She apparently has not been incapacitated although she suffers from severe headaches every morning. It is possible that she will become incapacitated because of the brain damage. I told Mr. Neugass we should have a copy of Mrs. Neugass' Will. Mrs. Neugass has no assets of significant value.

I suggested the following alternatives to Mr. Neugass with respect to the art:

a. Outright bequests. I pointed out that this would involve a substantial estate tax cost and would in effect require the estate to "buy back" the paintings.

b. Life interests in the paintings, with remainders to a Foundation to be established.

c. An outright bequest of the paintings to a Foundation to be established.

Mr. Neugass mentioned that certain charities now are taking the paintings and are agreeing to loan the paintings back to the donors at a nominal charge. I told him that I did not think that this would be a procedure which we could sanction from the point of view of obtaining an income tax deduction for the present gift. I told him, however, that I would look into it further.

Could we do the following with the works of art:

Leave the works of art to the wife for life with the power to renounce in whole or in part within three months after death, the remainder to the daughter with the power to renounce in whole or in part, including the power to cut down the interest to a life interest. In the event of renunciation by wife and daughter, the works of art would pass to the Foundation. The Foundation would be established now and qualified. The Foundation would be for general charitable purposes. The advantages of this procedure as I see it are as follows:

The wife would have the life use of such works of art as she should choose at a cost of the estate tax on the life estate. The daughter could determine whether she would have a life interest in the works of art, have the works of art outright, or have the works of art go into the Foundation. If the wife were alive at Mr. Neugass' death, arrangements would have to be made for the payment of estate tax on any works of art to be retained by the daughter.

I have the following additional thoughts with respect to the paintings:

a. Mr. Neugass should consider a program of gifts of undivided interest in the paintings of \$6,000 a year to his daughter.

b. Should we suggest grants to museums of interests in the paintings for terms of years, either presently for income tax purposes, or under his Will to reduce estate taxes?

c. If we are to set up a Foundation now and if the Foundation were in the home of the daughter, could we reasonably keep paintings in her home when such paintings were not on loans to museums if we in fact made bona fide efforts to keep the paintings on loan or in public view at all times

I would like to chat with you briefly before we proceed in getting up a first draft of the Will.

ASR